IN THE

Supreme Court of the United States

NOVEMBER TERM, 1978

No. 78-869

In the Matter of

STIRLING HOMEX CORPORATION,

Debtor.

GREGORY JEZARIAN, GERALDINE JEZARIAN, LONETOWN COMPANY, HARRY E. JONES, ALECK GOLDBERG, as Custodian for MARK GOLDBERG, and MRS. D. WINDSOR DIXON,

Petitioners,

—versus—

FRANK G. RAICHLE, Reorganization Trustee; LINCOLN FIRST BANK OF ROCHESTER; CHEMICAL BANK; THE CHASE MANHATTAN BANK, N.A.; THE FIRST NATIONAL BANK OF CHICAGO; MARINE MIDLAND BANK; THE TRAVELERS INDEMNITY COMPANY; and THE SECURITIES AND EXCHANGE COMMISSION,

Respondents.

PETITIONERS' REPLY BRIEF

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December 29, 1978

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The briefs of Trustee Raichle and of Chemical Bank and The First National Bank of Chicago, the only ones thus far served on petitioners, have no answer to our submission that equitable subordination of claims of innocent creditors is without precedent and that authority in this Court and in appeals courts in other circuits is all to the contrary. Instead, respondents urge that the question presented involves facts and complications which are unmentioned in the petition (as well as being disregarded in the opinions below).

Respondents' points are specious.

Response To Trustee Raichle

1.

The Trustee, br. p. 2, suggests that the District Judge's "discretionary" subordination of petitioners' claims is based on facts and evidence peculiar to this proceeding.* In actuality the opinions below amount to judicial declarations that, in *any* Chapter X liquidation-reorganization, fraud claims, for no reason other than that they are asserted by present or past stockholders, rank below all other unsecured claims.

2.

In relying on § 510(b) of the Bankruptcy Reform Act the Trustee, br. p. 4, conveniently overlooks that it does not take effect until October 1, 1979 and then only with the strongest possible saving clause for pending proceedings; pet. p. 5. To establish that § 510(b) "is merely a codification of existing law" the Trustee, br. pp. 5-6, resorts to inapposite citations: *F.D.I.C.* v. *American Bank Trust Shares, Inc.*, 412 F. Supp. 302 (D. So. Car. 1976), vacated and remanded, other issues, 558 F. 2d 711 (4th Cir. 1977), was a receivership, not a bankruptcy; in *Carter* v. *Bogden*, 13 F. 2d 90 (8th Cir. 1926), and *In re Groenleer-Vance Furniture Co.*, 23 F. Supp. 713 (W.D. Mich. 1938), the claimant-stockholders were not innocent of fraud like petitioners but themselves had overreached the debtor; and the rationale of *Scott* v. *Abbott*, 160 Fed. 573 (8th Cir.), *cert. den.* 212 U.S. 571 (1908), that stockholders were estopped to assert fraud claims against the debtor because its recreant officers were *ex officio* the agents of the stockholders, was implicitly

* In similar vein the Banks' brief, pp. 8-13, presents a lengthy Statement of the Case, virtually none of which is germane either to the reasoning below or the issue presented by the petition.

rejected twenty-nine years later when this Court allowed such claims on a parity basis, *Oppenheimer* v. *Harriman National Bank & Trust Co.*, 301 U.S. 206 (1937).

3.

The Trustee, br. pp. 10-11, tries to distinguish *Oppenheimer, supra,* on the ground that it arose under the National Bank Act, 12 USC § 194, which calls for "ratable" distribution, as against Chapter X of the Bankruptcy Act, §§ 174, 221(2), 11 USC §§ 574, 621(2), which provides for "fair and equitable" distribution. But "ratable" in the Bank Act means "'just and equal' . . . through the operation of familiar equitable doctrines." *American Surety Co.* v. *Bethlehem Bank*, 314 U.S. 314, 316 (1941). Compare *Case* v. *Los Angeles Lumber Products Co.*, 308 U.S. 106, 115-116 (1939); *Caplin* v. *Marine Midland Grace Trust Co. of New York*, 406 U.S. 416, 436 n.2 (1972). The ultimate standard under both statutes is the same.

4.

According to the Trustee, br. p. 7, petitioners, "except for a negligible few," waited too long to assert their claims. The suggestion underlying this statement is that a bar order obtained by the Trustee in December 1972, soliciting claims "of whatever character . . . other than those founded on . . . shares of stock", encompassed stockholders' fraud claims.* Petitioners' position has been that this verbiage was not adequate notice that such claims were about to be barred, and that they have yet to be called for. See *City of New York* v. *New York, New Haven & Hartford Railroad Co.*,

* The order is more fully referred to in the opinion below; pet. 7a, n.5, 2d ¶.

344 U.S. 293, 297 (1953). Notwithstanding extensive argument of this question, the District Judge, pet. 24a, left it unmentioned, and the court below, pet. 7a, n.5, 2d ¶, declined to discuss it.

Response To Chemical Bank and the First National Bank of Chicago

The Banks' main effort, quite unlike the Trustee's, is to justify subordination of petitioners' claims on the theory, br. p. 14, "that claims such as those asserted by Petitioners are neither provable nor allowable in a liquidation bankruptcy proceeding." The Banks, br. p. 14, cite four cases for this proposition: *Bizzell* v. *Hemingway,* 548 F. 2d 505 (5th Cir. 1977), and *Duban* v. *Pro-Tech Programs, Inc.,* 441 F. Supp. 467 (S.D.N.Y. 1977), were both Chapter XI arrangements, while *In the Matter of Cartridge Television, Inc.,* 535 F. 2d 1388 (2nd Cir. 1976), and *In the Matter of Frank J. Crimmins,* 406 F. Supp. 282 (S.D.N.Y. 1975), were straight bankruptcies.

At most these cases stand for the non-provability of fraud claims under §§ 17(a), 63(a) and 371 of the Bankruptcy Act, 11 USC §§ 35(a), 103(a) and 771, applicable in such proceedings. Those provisions, hence those citations, have no application to a Chapter X proceeding. Section 106 of Chapter X, 11 USC § 506, which the Banks omit to mention, defines "claims" to "include all claims of whatever character

. . . whether or not such claims are provable under section 63 of this Act . . ."; the same section defines "creditor" as "the holder of any claim." The Court of Appeals, pet. 12a-13a, assumed, for purposes of its opinion, that petitioners are creditors. The Banks have no effective authority to the contrary.

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Respectfully submitted,

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